IN THE

Supreme Court of the United States

OCTOBER TERM, 1949

No. 785

PRUDENCE-BONDS CORPORATION (NEW CORPORATION),
Petitioner,

against

SAMUEL SILBIGER, et al.,

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT WEIL, GOTSHAL & MANGES, IN OPPOSITION

Opinion Below

The opinion of the court of appeals for the second circuit is as yet unreported but appears at R. 755-787. The opinion of the district court appears at R. 318-322.

Jurisdiction

The decree of the circuit court of appeals was entered on March 7, 1950 (R. 765). Petitions for rehearing filed in that court were denied on April 5, 1950 (R. 786). The jurisdiction of this court is invoked under Section 240(a) of the Judicial Code, as amended, 28 U. S. C., Section 347(a) and Section 24(c) of the Bankruptcy Act, as amended, 11 U. S. C., Section 47(c).

Questions Presented

The questions presented, insofar as they affect respondent Weil, Gotshal & Manges, are:

(1) Assuming a client had two interests in conflict with each other, can an attorney, who was retained for and served only one of those interests, served that interest loyally and served no other interest, be held to have served conflicting interests so as to require the denial of compensation to him?

(2) Does the Bankruptcy Act require the denial of any allowance of compensation to an attorney whose client, without the knowledge of the attorney, purchased and sold securities of the corporation in reorganization?

Statute Involved

The Bankruptcy Act, as amended, provides in pertinent part:

SECTION 242 (11 U. S. C. Section 642). "The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in connection with the administration of an estate in a proceeding under this chapter * * *

* * * * *

"(2) by any other parties in interest * * *; and

"(3) by the attorneys * * * for any of the foregoing * * *."

SECTION 243 (11 U. S. C. Section 643). "The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred by creditors * * * and the attorneys for any of them, * * * in connection with the administration of the estate. * * *."

SECTION 249 (11 U. S. C. Section 649). "* * * No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred. * * *."

Statement

Respondent Weil, Gotshal & Manges has been awarded an allowance of $20,000 for its services in the "Construction Proceeding".[1] That proceeding was necessary in order to determine whether a "surplus", existing in the principal accounts of certain of the bond series, should be used to pay interest in full on the publicly held bonds of those "surplus" series in accordance with their original tenor, or should be allocated to the payment of subordinate bonds in the "surplus" series, and any balance remaining thereafter, prorated among the so-called "deficit series". Determination of this question meant a gain or loss to the public bondholders of the Fifth Series of $360,610.22, and a gain or loss to the public bondholders of all the "surplus" series of $1,994,453.79 (R. 168-169).

Until this problem arose, the public bondholders of all series (both "surplus" and "deficit" series) had no divergent interests. Accordingly, the New Corporation (the petitioner herein) was able to and did act on behalf of all series. However, when this problem of construction arose, the New Corporation took the position that it must remain neutral by reason of the divergent interests of "surplus" series on the one hand, and "deficit" series on the other (R. 288). It thus became necessary for those

[1] The petitioner has set forth a brief summary of the various proceedings in this Reorganization at pp. 4-9 of the petition. The details of the Construction Proceeding appear at pp. 6-9 of the petition.

bondholders who desired to protect their interests to intervene in the proceedings (R. 359).

Respondent Weil, Gotshal & Manges was retained by James L. White and several other public bondholders to intervene in the Fifth Series (a "surplus" series) in which they held bonds. This respondent thereupon took the position that the publicly held bonds in each series were entitled to be paid interest in full, in accordance with their original tenor, before there could be any surplus for distribution to subordinate bondholders in the particular "surplus" series, and "deficit" series bondholders thereafter (R. 260-264). The special master to whom the matter was referred took a contrary view in which position he was sustained by the district court. An appeal from the order of the district court was taken by this respondent Weil, Gotshal & Manges and by respondent Samuel Silbiger (R. 265). No other attorneys so undertook to protect the rights of the public bondholders of the "surplus" series. On appeal, the court of appeals for the second circuit reversed the district court and held that the publicly held bonds were entitled to full interest in accordance with their original tenor. At this point in the proceeding, the petitioner, who had asserted that it must remain neutral, joined in a petition to this court for the granting of a writ of certiorari. Again, only respondent Weil, Gotshal & Manges and respondent Silbiger defended the rights of public bondholders of the "surplus" series by opposing the granting of the writ. This court denied the petition.

Thereafter, the matter of the present allowances came on before the district court and was referred to a special master for the taking of testimony. At the hearings before the special master the following pertinent facts with respect to respondent Weil, Gotshal & Manges were disclosed and were in no respect disputed:

(1) Respondent Weil, Gotshal & Manges was retained and appeared in the Fifth Series only (R. 609-610, 353, 355, 571-572).

(2) Respondent Weil, Gotshal & Manges at all times advocated the claims only of the Fifth Series public bondholders (R. 351).

(3) Respondent Weil, Gotshal & Manges had no knowledge of its client's bond holdings in series other than the Fifth until immediately prior to the hearings on allowances (R. 570-571).

(4) Neither respondent Weil, Gotshal & Manges, nor any member of that firm, traded in the securities of the debtor corporation (Petition, p. 20).

(5) Respondent Weil, Gotshal & Manges had no knowledge that its clients had traded in the securities of the debtor corporation until immediately prior to the hearings on allowances (R. 570-571).

Argument

Petitioner claims that the allowance awarded to respondent Weil, Gotshal & Manges (and we here restrict ourselves solely to that respondent) is improper on two grounds, firstly, that this respondent served conflicting interests, and secondly, that Section 249 of the Bankruptcy Act requires the denial of any allowance to this respondent.

1. The Charge of Conflict of Interests

It is contended by the petitioner that, in view of the fact that the clients of respondent Weil, Gotshal & Manges owned bonds in both "surplus" and "deficit" series, these clients had conflicting interests; since respondent Weil, Gotshal & Manges served these clients, they necessarily served "conflicting" interests. Hence, it is claimed, under the doctrine of *Woods* v. *City National Bank & Trust Co.*, 312 U. S. 262, compensation should be denied this respondent.

This argument is utterly fallacious. True, the clients of this respondent held bonds in both "surplus" and "deficit" series. They chose to press the claims of one of these interests. Thus, it is undisputed that this respondent was retained by its clients to represent them as bondholders of the Fifth Series only, and instructed this respondent to take the position it did. Respondent represented bondholders of no other series. Moreover, petitioner concedes (Petition, p. 10) that Weil, Gotshal & Manges "confined their activities in the Construction Proceeding to the Fifth Series" and, again, that Weil, Gotshal & Manges "advocated in the Construction Proceeding the side of the surplus series" (Petition, p. 11). This respondent thus served the interests of their clients only insofar as they held bonds in the Fifth Series. (In fact, as appears above, this respondent knew of no other interests of their clients.) By so doing, it served the interests of all bondholders of the Fifth Series as well as all other "surplus" series. It did not "serve individual interests in conflict with the interests of the class" (public bondholders of "surplus" series) as petitioner claims (Petition, p. 21). On the contrary, the individual interests (i. e., Fifth Series interests) served by respondent Weil, Gotshal & Manges were identical with the interests of the class.

The fact that the clients held bonds in other series in no way affected the representation by Weil, Gotshal & Manges of their interests in the Fifth Series. Weil, Gotshal & Manges retained only in the Fifth Series, served one master only, a Fifth Series master and served that master consistently, undividedly, and well (R. 267). The propriety of this respondent's behavior, under these circumstances, cannot be questioned.

2. Client's Dealings in Securities of the Debtor

The second contention made by petitioner is that since the clients of respondent Weil, Gotshal & Manges traded in the securities of the debtor during the pendency of the proceeding, Weil, Gotshal & Manges should be denied compensation in accordance with Section 249 of the Bankruptcy Act.

This contention is equally without foundation. Section 249 denies compensation to

> "any committee or attorney, or other person acting in the proceeding in a representative or fiduciary capacity, who, at any time after assuming to act in such capacity, has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred."

Respondent Weil, Gotshal & Manges here seeks compensation in its own right by virtue of Sections 242-243 of the Bankruptcy Act. It is undisputed that neither respondent Weil, Gotshal & Manges, nor any member of that firm traded in the securities of the debtor (Petition, p. 20). Petitioner seeks to have compensation denied to said respondent on account of trading, unknown to respondent, by the clients.

Of course, any disability visited by Section 249 is a personal disability, extended only in rare instances to the trading of a wife or partner on the basis of the assumed benefit to the applicant. No case is cited by petitioner for the proposition that an attorney must be denied compensation on account of trading by his client. Moreover, in the case cited by petitioner to buttress its contention, the chairman of a committee was denied compensation for having himself traded in the securities of subsidiaries of the debtor corporation. Yet, this prevented neither

the remaining members of the committee nor the attorneys representing the committee from being awarded compensation. (*In re Midland United Company,* 64 F. Supp. 399, affd. 159 F. (2) 340.)

Again, in *In re Mortgage Guarantee Company* (40 F. Supp. 226, 237, 238), the disability of a client by virtue of Section 249 was specifically held not to extend to that client's attorney who was allowed compensation. This view of the statute is approved by leading authorities. Thus, it is stated in Collier on Bankruptcy, Vol. 6, 14th Edition, p. 4592:

> "The fact that a representative of creditors is barred from an allowance by virtue of § 249 will not prevent the making of an allowance to its counsel who has not participated in any transfers prohibited by the section, * * *."

We submit that the position advocated by the petitioner is clearly not the law. If, indeed, it were, it would only be in the rare situation that the interests of small creditors and minority groups would be protected in a situation such as arose in the instant case. Clearly, if attorneys had here known that they might be deprived of any allowance because, unknown to them, their clients held securities in other series or traded in securities of the debtor, they would have been extremely reluctant to embark on proceedings which have been as protracted as this proceeding.

The present Bankruptcy Act, and more particularly its revisions with respect to allowances, was intended to democratize reorganization proceedings by encouraging the participation of small creditors and minority groups. Such groups could rarely obtain representation if petitioner's contentions were sound. Obviously, small creditors could not undertake to compensate counsel fully for their services in complicated and protracted proceedings of this kind. Consequently, the Bankruptcy Act in order to assure such representation, provided for payment of attorneys' compensation out of the estate. But, if petitioner's position

is correct, the purpose of the latter provision would be nullified. Few attorneys would undertake such representation where an allowance was wholly dependent on the acts of a client beyond control of the attorney. As Judge Learned Hand said in the court below:

> "To charge him with his client's dealings would compel him, at the risk of losing all his labor, either to keep an eye upon those dealings (which in practice would be so irritating as to imperil the continuance of their relations); or blindly to put any right to be paid at his client's mercy."

Actually, mere "watching" of the client would be of no avail. No attorney could be expected to prevent a client from purchasing securities of the debtor where the client was determined so to do.

We submit that the petitioner's contentions find no support in either the applicable statutes or the pertinent decisions. Furthermore the acceptance of such contentions would lead to such absurd results as to demonstrate the complete fallaciousness of its position. For, if respondent Weil, Gotshal & Manges represented the entire class of publicly held bonds in all "surplus" series, as necessarily contended by petitioner, then said respondent would be debarred from any allowance if any of the thousands of public bondholders of the entire class traded in the bonds of any series or even owned a single bond in one of the "deficit" series.

Conclusion

This brief has been restricted to the questions presented insofar as they relate to respondent Weil, Gotshal & Manges. We respectfully submit that in view of the lack of conflict on these questions and in view of the fact that petitioner's contentions with respect to these questions raise no issues which require further review by this Court, certiorari should be denied in respect to respondent Weil, Gotshal & Manges.

WEIL, GOTSHAL & MANGES,
Respondent.

FRANK L. WEIL,
EDWARD C. WALLACE,
MILTON HASELKORN,
of Counsel.

May, 1950.